PRICE MAINTENANCE

The arguments advanced for and against the maintenance of resale prices fixed by manufacturers have in the vast majority of cases been put forth by interests which expected to be directly affected by legalized price maintenance. In comparatively few instances has the subject been considered in a scientific manner as a problem in economic policy. Little distinction has been made as to the various forms and motives of price cutting; while disapproval of predatory price cutting and of fraudulent advertising has been taken to mean approval of the legalization of price maintenance as a remedy.

Consumers' interests will in the long run be determining for or against the legalization of price maintenance. The consumer desires to satisfy his wants with minimum expense and effort. But in order that this may be brought about, adequate compensation for necessary producers must be provided, whether manufacturers or distributors. The long run interest may not conflict, but there may certainly be disagreement as to policy at any time among the various classes, manufacturers, distributors or consumers; such friction is inevitable. But no one interest can be seriously affected without ultimately influencing the welfare of the others. To justify a radical change in marketing conditions, net positive benefits to the public should reasonably be expected. And the burden of proof may fairly be said to rest upon the advocates of a change, the effects of which cannot be predicted with any degree of certainty. Proponents will have justified their position from the viewpoint of public policy when they have demonstrated, first, that price maintenance offers positive advantages and, second, that possible disadvantages are not more detrimental than abuses under the present system. Before proceeding to the crucial question of consumers' welfare, the interests of manufacturers and middlemen will be examined.

Price Maintenance and the Manufacturer[1]

A system of fixed resale prices is favored by some manufacturers of identified articles because it seems to offer assurance of greater stability of profits. Price cutting is said to decrease the

[1] The repetitions of arguments and statements are so numerous both in the press and in the various hearings that no attempt is made in the subsequent discussion to give an extended list of specific references. Upon the attitude and interest of manufacturers in price maintenance may be consulted F. W.

volume of sales, therefore profits, and the manufacturer does not secure the returns to which he is entitled. Through persistent advertising, the maintenance of standards of quality, or otherwise, the manufacturer has built up a reputation or fund of goodwill; customers prefer the article of his manufacture to other similar articles. But the value of the article is said to be associated with its price; any reduction of price tends to leave the impression with the consumer that the article is not as desirable as before. From the viewpoint of the manufacturer this has two injurious effects. First, his goodwill is impaired because the customer ceases to prefer the article upon which the price has been cut. In the second place, the decline of consumers' demand and the lowering of the margin to retailers prejudices the dealers against the article; they refuse to handle it, or at least their interest in "pushing" it has declined. In these ways the volume of manufacturer's sales is unfavorably affected, his profits are decreased and the value of his goodwill is diminished. Therefore an enforceable plan of preventing price cutting, namely legalized price maintenance, is declared to be necessary in order to secure to the manufacturer the return upon goodwill to which he is entitled.[2]

The general validity of the protection to goodwill argument for price maintenance is questionable. To possess force it must be based upon three propositions: (1) that predatory price cutting has materially deprived manufacturers of the benefits of

Taussig in the American Economic Review, vol. VI, no. 1, Supplement, p. 171 *et seq.*; L. H. Haney, *ibid.*, pp. 188-190; W. F. Gephart, *ibid.*, p. 192; also Gephart, *Some Economic and Legal Aspects of Fixed Prices*, pp. 164, 170. The testimony of W. H. Ingersoll of the Robert H. Ingersoll Company, Sydney M. Colgate of Colgate and Company, and Henry C. Brown of the Victor Talking Machine Company represents the attitude of the manufacturers, in the recent hearings before the Federal Trade Commission (reported in *Women's Wear*, beginning October 5, 1917), as well as in the various hearings before congressional committees. The titles of the printed reports of these committee hearings are given in note 1 on page 28 of vol. VIII (March, 1918) of this Review.

[2] It is evident that those manufacturers known as national advertisers are most interested in the legalization of price maintenance. Manufacturers who are unable or unwilling to undertake extensive advertising as well as manufacturers of unidentified products have no direct interest in the goodwill of the sort depending upon maintained prices. Statistics are not available as to the proportion of goods identified by trade-marks or otherwise. Rough estimates have placed the amount of branded goods in hardware and department stores at from 5 to 10 per cent; while it seems that the proportion is somewhat higher in the grocery and drug trades.

their goodwill, (2) that such deprivation of goodwill is socially undesirable, (3) that price maintenance is the proper remedy. Evidence seems to be contrary to the assertion that manufacturers have suffered. The differential advantage called goodwill may occasionally be built up upon the basis of advertising, without substantial merit of product or service to consumer. And it is believed that such predatory price cutting as does take place should be reached by other means than legalization of price maintenance.

The normal consequence of reduction in prices is an increase in volume of sales.[3] But reasoning theoretically it is conceivable that price cutting might result in decrease of a manufacturer's sales. In order that this be brought about, either the demand for the goods must diminish or the existing demand must be less completely satisfied than before. Diminished demand would follow reduction in price only when the goods were of the sort which possess a value associated with price, a distinction value which is lessened when the price is lowered.[4] The idea of exclusiveness or superiority impressed upon the minds of consumers by persistent advertising is an uncertain quantity, and may be weakened by price cutting in certain cases; although the social benefit of artificially creating a value which cannot withstand price cutting is doubtful. It may be seriously questioned if an article of merit will ever be injured by price cutting.

As to the second point, it does not seem that ordinarily the machinery for satisfying consumer demand would be so affected that ultimate restriction of manufacturers' sales would follow. The attitude of retailers toward an article upon which prices are cut is undoubtedly an important factor in affecting the volume of sales. If they consider the cut prices so low as not to give them the customary profit, jobbers and manufacturers may in turn be asked to shade prices, and may not be inclined to urge sales of the

[3] Upon the effect of price cutting upon sales of advertised articles, see testimony of Homer S. Ames, Edward A. Wise, and H. B. Cheney before the Federal Trade Commission, reported in *Women's Wear,* Oct. 4, 30, and Nov. 16, 1917; also O'Donnell in *Printer's Ink,* Jan. 20, 1916, p. 47; and thesis written by Mr. Raymond B. Callahan upon basis of questionnaire to housewives of New York City. Further consult J. R. Turner, AMERICAN ECONOMIC REVIEW, vol. VI, no. 1, Supplement, p. 198; Report I, pp. 11 *et seq.* (testimony of Mr. Louis Brandeis); and Report II, p. 6 (testimony of Dr. P. H. Nystrom).

[4] F. W. Taussig, *Principles of Economics,* vol. I, p. 130.

article. That they will generally refuse to handle it is open to question. Advertising by manufacturers direct to consumers is undertaken for the purpose of creating "consumer demand," the creation of which is looked upon as a method of securing influence over middlemen; a recognition of the fact that retailers must carry in stock what consumers demand. If that is true, price cutting upon a superior article known to consumers will not eventually restrict the distribution of an article, because the customer will continue to demand it; in the long run it is no less necessary for middlemen to serve the public than for manufacturers.[5]

As in the case of many broad problems in economics, verification of theoretical conclusions is a difficult matter. The conspicuous absence of statements of fact in discussions of price maintenance lays both proponents and opponents open to criticism. There seems to be little indication in the evidence that business men in general, including manufacturers, have been much harmed by price cutting. Advocates of price maintenance picture price cutting as a business practice which will have disastrous results upon all interests; opponents, on the other hand, assert that price cutting of the predatory sort is only a sporadic occurrence.[6] That unfair price cutting takes place is not open to question; but there is wide variation of opinion as to its extent and results.[7] Chal-

[5] There are certain practices common among the advocates of price maintenance which have as much bearing upon the character of the distributive system as price maintenance or price cutting. Quantity discounts given to the large retailers, or jobbers' discounts given to certain retailers who may or may not be in the jobbing trade besides, furnish an argument for variations in retail selling prices, place the small retailer at a disadvantage in buying, and therefore, from the point of view of the manufacturer, tend to have the same effect upon the distributive system as price cutting.

[6] As far as the consumer's appraisal of an article is concerned, both those cut prices resulting from honest endeavor of the distributor to share the effects of lower costs with the public and the cut prices for the purpose of attracting customers and selling them other articles of doubtful value tend to have the same effect. The motive of the retailer in the latter case is not published.

[7] The majority statement of the Committee of the Chamber of Commerce of the United States says that it has records of "literally hundreds of cases of damage inflicted upon the interests of manufacturers, wholesalers and small retailers." But absence of detail is conspicuous here, as well as in the voluminous testimony before congressional committees and the Federal Trade Commission. *Report of Committee of Chamber of Commerce of the United States on Maintenance of Resale Prices*, p. 21. The minority statement (*ibid.*, p.

lenges of opponents to produce instances of actual injury to articles of merit by price cutting have not, as far as can be ascertained, been satisfactorily answered. Statistics of failures and balance and income sheets of national advertisers which strongly advocate price cutting, as well as of those which are non-committal, give no evidence that price cutting has been disastrous to manufacturing interests. The dividend rates vary widely, some showing small or moderate profits, others very large; while goodwill and trade-marks were in some instances capitalized at huge sums, upon which dividends were paid.[8]

That price maintenance, at least temporarily, offers greater assurance of stable profits and sales to manufacturers of identified articles who have already built up goodwill may be granted. But it also offers greater resistance to new manufacturers who

14) contains the following assertion, "The Minority Committee has been unable to ascertain one well defined case of the failure of either a manufacturer, jobber or retailer resulting from price cutting on identified goods. Nor have they been able to establish that the sales of any well known articles have been stopped or its popularity been injured by price cutting." In the testimony before the Federal Trade Commission, October and November, 1917, Professor Samuel McCune Lindsay arguing against price maintenance speaks of unfair price cutting as "incidental." Reported in *Women's Wear,* Oct. 4, 1917. *Cf.* L. H. Haney, AMERICAN ECONOMIC REVIEW, vol. VI, no. 1, Supplement, p. 190.

[8] It seems that if price cutting were very common and disastrous to business, such effects would be reflected in the statistics of failures during the past few years. Statistics issued by the Bradstreet Company in *Bradstreet's Journal,* January 27, 1917, show that the percentage of business enterprises failing in 1915 was 1.17, in 1916, .92. Of these *Bradstreet's* assigns as due to competition 5.7 per cent in 1915, and 4.2 per cent in 1916; that is, of the total number of business enterprises, six hundredths of one per cent failed in 1915 because of competition, and in 1916 less than five hundredths of one per cent. Under competition are included forms which could not be classed as price cutting. Making wide allowances for faultiness in classification and inaccuracies in figures, there is nothing to indicate that business men as a whole, either manufacturers or distributors, have suffered business disaster from price cutting to any extent. The percentage of failures is no greater in 1917 than it was prior to 1900.

Information as to earnings of manufacturers of identified articles now on the market as compared to other business concerns does not give much light upon the question. Some of the most active proponents of fixed resale prices are closed corporations upon which few data are published. The general impression gained by the writer from the examination of a large number of published statements of financial conditions found in *Moody's Manual of Industrial Securities,* 1917, was that as a rule the makers of advertised products were prosperous.

wish to enter the field.[9] Necessarily a new manufacturer must procure larger means in order to establish himself against powerful competitors. He must advertise extensively. If, as advocates of price maintenance claim, competition would not be lessened, some new firms would be successful in breaking into the market, involving restriction of the sales (or decrease of return upon goodwill) of those already in the field. On the other hand, if the hold of the existing firms on the market is sufficiently strong to prevent newcomers from obtaining a foothold, it would seem that such protection as is afforded by price maintenance would neither be needed from the viewpoint of the manufacturers of identified articles themselves nor be advisable from the viewpoint of public policy, as tending to increase monopolistic control of the market. That legalized price maintenance would not give manufacturers operating under it a monopoly because the consumer will not continue to buy articles which are not satisfactory both in quality and price involves two assumptions;[10] namely, that substitutes are available and that the consumer is a competent judge. For many articles, especially those protected by patent or copyright, no substitute is available; while the difficulty of dislodging an already established producer of trade-marked articles operates likewise to prevent the increase of substitutes. The second assumption, that the consumer is a competent judge, may not be incorrect, but it is inconsistent with the statements that price maintenance is necessary to prevent "price cutters" from palming off inferior goods upon the public at high prices.

Lastly, it seems that price maintenance as a policy would have little effect in the direction of lowering costs of manufacture. The only methods by which costs could be decreased would be (1) by the better utilization of existing capacity, either by more complete utilization[11] or increased efficiency; and (2) by increasing the scale in such industries as are subject to the law of increasing returns. There is little reason to believe that price maintenance would lessen costs in either manner. In the first place, if price

9 William F. Gephart, *Some Economic and Legal Aspects of Fixed Prices*, Washington University Studies, vol. II, pt. II, no. 2, April, 1916, p. 165.

10 Gephart, *Some Aspects*, etc., pp. 165-166.

11 If competition between manufacturers is not decreased, so that something akin to monopoly is operative, continued full utilization of capacity would be no more likely to occur under price maintenance than under present conditions. There is nothing in price maintenance *per se* to bring a closer adaptation of industrial equipment to needs.

maintenance were to become legalized, and identified goods much more common,[12] the share of a particular concern would be determined by its success in securing the goodwill of consumers and distributors. The average size of the manufacturing unit would depend upon the proportion of national income expended for the particular article and the number of establishments among which the income was divided. The share of the average income expended for particular articles might be influenced by advertising, but with typical incomes of the country moving as slowly as they do, the diversion of income to a particular type of expenditure through the influence of advertising would imply a decrease, or at least a lack of increase over considerable periods in the expenditures for other articles; so that the increased scale of production which might result from extensive advertising by numerous competitors in one line would be accompanied by a standstill or decrease in the efficiency and scale of enterprise in other lines. Within a particular industry, an increase in the size of the average manufacturing enterprise could take place only by an increase in the total demand or decrease in the number of concerns.[13] Even if we assumed as possible an increase in the total demand for identified articles under a widely adopted system of price maintenance, there still remains to be proved the extent of the economies of large-scale production, a point upon which students of industrial organization are at present inclined to be more skeptical than in times past.

In the second place, if price maintenance assures manufacturers of the benefits of goodwill they have created through profits

12 In discussions of legalized price maintenance it should be fair to assume that manufacturers as a class desire to avail themselves of its provisions. A great increase in identified articles would be the result. If few manufacturers employ the price maintenance policy or desire to employ it, such legislation is open to the charge of class legislation. If they do use it, then the advantage to the consumer of standardized products is in part loss, because it is necessary for him to choose between a large number of competing products; likewise it becomes more difficult and more expensive to create goodwill for competitive products.

13 In other words, the only way in which the average size of the business unit could be increased, unless competition were decreased, would be as a consequence of the increase in total demand for a particular class of identified article. Such increase would be brought about with difficulty, because of the comparative fixity of real incomes over considerable periods, the ever increasing variety of identified goods, the ever increasing variety of desires, and the welcome given the new articles.

considered by them to be satisfactory, it might also have a dulling influence upon the progress of the particular branch; because the need of constant alertness for change in the search for greater efficiency in order to maintain profits would be less pressing. Consequently it seems that price maintenance would have little influence upon bringing greater efficiency into manufacture, and therefore lower costs.[14]

Price Maintenance and Middlemen

a) Wholesalers.[15] Middlemen other than retailers have not assumed a prominent part in the price maintenance movement. Some few wholesalers have expressed their approval of the measure; some their opposition. Their general silence is probably due to their desire to avoid the antagonism of manufacturers and retailers who may be actively interested. The interest of wholesalers will rest in part upon their convictions as to the probable effect of legalized price maintenance upon the retailers to whom they cater. If they believe that price cutting tends to eliminate the small independent retailer, and that price maintenance is a remedy, they may favor it as a means of retaining their clientèle; the more, if they think that price cutting encourages the development of the newer types of retailers who attempt to pass over the jobber and buy directly from the manufacturer at jobbers'

[14] "It has not yet occurred to some of those who are frantically engaged in tampering with economic laws for the sole purpose of getting some of the national advertising that pays well, that there is already a very serious problem in wholesale dry goods markets growing out of the very thing they are trying to force upon the retailer, and which the retailer has succeeded in part in forcing on mills. That is, the stifling of initiative and individuality in fabrics by demandng that they shall be made to sell at certain fixed prices, say, 19c, 25c, 39c and so on. Those who have studied the genesis of this trouble are convinced that the fixing of prices in this way has fixed American textile development in limited channels." New York *Journal of Commerce and Financial Bulletin,* Nov. 19, 1915. Mr. E. A. Filene testifying before the Committee on Interstate Commerce, Jan. 6, 1917 (Report III, p. 209 *et seq.*), stated that legislation to legalize price maintenance was contrary to the best interest of manufacturers themselves because it made the manufacturers depend upon the support of paternalistic law rather than upon their own strength.

[15] A limited amount of material upon the position of wholesalers may be found in Report I, pp. 283 *et seq.*, 287 *et seq.*, 292; Report II, p. 19; W. F. Gephart, *Some Aspects*, etc., p. 171. Testimony before the Federal Trade Commission by Mr. Colgate, reported in *Women's Wear,* Nov. 2, 1917.

prices.[16] Likewise the jobber might favor price maintenance as a means of relieving him of demand for reduced prices by customers affected by price cutting. On the other hand, jobbers who believe that the retailer would not be injured by price maintenance, or who object to restriction would not register approval. The position of some jobbers as manufacturers or sellers of private brands would affect their attitude; since as distributors they might not be able to compete in advertising with manufacturers' brands, any movement to strengthen these brands would meet with disfavor. Assuming that they were able to advertise on an equal scale with manufacturers, their closer contact with retailers would render statutory legalization of price maintenance less necessary should they incline toward fixed prices.

If manufacturers generally availed themselves of the privileges granted them by a price maintenance statute to fix prices to wholesalers and retailers, the margin to wholesalers would thereby be fixed, regardless of differences of expense of handling business, and, in the absence of quantity discounts, regardless of the volume of goods handled. With a margin lower than the customary, there would be greater incentive to increase the number of private brands and to push these to the exclusion of the manufacturers' brands upon which prices were maintained; otherwise only large jobbers would have a sufficient volume of business to continue. If the margin allowed were comparatively high, incentive to improvement in methods would be lessened, because average efficiency would bring satisfactory returns. The precarious position of the wholesaler in certain lines at the present time seems in part to have been the result of his inefficiency. Competition, in the dry goods wholesale trade for instance, has resulted in the failure of some concerns, but it has necessitated the reorganization of others on more efficient lines.

Price maintenance ties the hands of the wholesaler more effectually than it does the retailer's. The wholesaler's recourse to additional service in selling to retailers is much more limited than that of the retailer in selling to consumers; consequently there would be a much nearer approach to suppression of competition, with the further result of decrease of incentive to greater efficiency, than would be probable in the case of retailing. The existence and justification of the wholesaler depends upon the effi-

16 Those jobbers who sell to the newer types or depend upon them for business would have less interest in the maintenance of the small independent.

cient rendition of his service; consequently any factor which tends to decrease that efficiency is in the long run detrimental to the wholesaler, even though temporarily it may give him larger profits and relieve him of the stress of competition.

b) Retailers.[17] Manufacturers interested in the continuance of their distributors in business, and the retailers themselves have repeatedly urged the legalization of price maintenance as a necessary measure for the protection of retail interests, especially of the small independent retailer. Though the lines are not clearly drawn, regular retailers ordinarily purchasing intermediately from manufacturers through wholesalers are more prominent among the advocates than chain stores, department stores, and mail-order houses. The situation has given rise to the statement that the question of fixed prices involves the problem of the large versus the small retailer, of the regular retailer as opposed to the newer types. The assertion follows that price fixation by manufacturers is the means of protecting the small retailer from elimination. That at first thought the fixation of prices seems desirable to the small retailer is unquestionable. Apparently it relieves him of all competition in prices with other retailers, as to identified commodities generally and also particular articles which may be used as leaders. It seems to him a more comfortable policy, one which will make his position and profits more secure. Competition is said to be placed upon a higher plane in that competition in service takes the place of competition in price. The retailer is relieved of all worry as to cut prices, the most direct method of cutting down his margin.

It seems that the position of the small retailer under conditions in which price and quality were fixed would eventually be no more secure than it is now. The idea that there can be competition dissociated from price is fallacious.[18] Competition in quality implies rivalry as to quality delivered for a certain price; competition in service implies rivalry as to amount and character

[17] The interest of retailers in price maintenance is considered in Report I, pp. 9, 41 *et seq.* (Mr. L. D. Brandeis); Report II, pp. 5, 7 (Dr. P. H. Nystrom), pp. 111, 117; Report II, pp. 248 *et seq.*, 310 *et seq.* (Mr. Wallace D. Williams), 209 *et seq.* (Mr. E. A. Filene), pp. 14 *et seq.* (Mr. Percy S. Straus), pp. 79 *et seq.* (Mr. J. M. Barnes); *Report of Committee of Chamber of Commerce of the United States,* pp. 16, 17, 26, 27.

[18] L. H. Haney, American Economic Review, vol. VI, no. 1, Supplement, p. 186; *Report of Committee of Chamber of Commerce of the United States,* pp. 21, 23.

of service rendered in delivery of goods of a certain quality at a fixed price. Comparisons of value mean nothing if either price or quality is omitted from consideration; the consumer purchases the commodity plus a certain amount of service offered by the distributor at a certain price. But at a given price there may be rivalry as to quality of the commodity or as to the amount of service to be sold with the material good. If in addition the quality is maintained at the same level by manufacturers, then the only rivalry of producers must be directed to the one remaining outlet, namely that of amount of service.[19] If certain types of retailers who sell at cut prices (except from malicious motives) are more efficient[20] than the small independent merchant, with maintained prices the former will be able to render greater service to the consumer as a means of attracting customers than the latter. Funds for advertising, probably swelled by maintained prices, would still be available for increased advertising, by which they could secure no less an advantage over the small retailer than they possessed before, though the public might not share in the benefits of their greater efficiency. In either case the disadvantage of the assumed inefficiency of the retailer would not be decreased. On the other hand, if the independent merchant is as efficient[21] or more efficient than the other types, he does not need

19 Service is here used to include all the various services rendered by retailers in the creation of time and place utility, not only in assembling and storing commodities, but also in delivery, in the extension of credit, and the numerous other conveniences offered by various retail establishments.

20 In so far as these retailers sell at cut prices because of lower buying prices from manufacturers (for the newer types of retailers frequently buy directly from the manufacturer), abolition of quantity discounts and special concessions often granted by manufacturer advocates of price maintenance would lessen the advantage of the newer types of retailers as opposed to small independents.

21 In the various hearings it is stated by the proponents of fixed prices that the small specialty store has lower costs of distribution than the department or chain stores; therefore, they should be retained in the distributive system as a matter of public policy; likewise it is stated that if chain stores and department stores parade cut prices, they must make up on other goods with higher prices quality for quality. Students of retail merchandising seem to be in essential agreement that the costs of doing business of the well managed specialty store are not higher than the costs of doing business of department stores. The cost of doing business in chain stores is declared by Dr. P. H. Nystrom, *Economics of Retailing*, p. 226, to be less than in average individually owned stores, though not as low as the best conducted individually owned stores. The same writer says (p. 199): "The department store has come into existence in response to an economic need. It has suc-

fixed resale prices in order to assure him his margin, provided sporadic unfair price cutting is controlled. The evidence is far from conclusive that price cutting, fair or unfair, has been the cause of serious injury to the small retailer.[22] On the other hand, it is scarcely probable that any type of small retailer could continue to use cut prices upon identified articles and indulge in the misrepresentations attributed to them, to attract trade, if the purpose were always what discussions of fixed price advocates seem to imply.[23] Fraudulent advertising, sometimes closely connected with price cutting, is an abuse which can be reached by other measures than price maintenance. And pressure of ultimate demand operates more directly upon the retailer than upon any of the other business interests concerned in price maintenance.

If fixed prices would deprive the retailer of the device of attracting trade by cut prices given with the purpose of bringing people into the establishment and selling them something else at a high price, it would likewise restrict the retailer in giving his customers extra benefits with the idea of increasing volume of sales with a lower rate of profit upon each turn, or sharing savings due to increased efficiency.[24] Cut prices are the most potent

ceeded and has continued to hold its place and to gain ground because it has occupied a certain point of advantage in the distribution of goods."

22 Dr. Nystrom quotes figures (p. 314) to the effect that 1.4 per cent of failures in the retail business are due to competition. As he remarks, the larger number of failures never reach bankruptcy proceedings and get into the records; but it is probably fair to assume that the causes of failure are operative with about the same force for those not reported.

23 Dr. Nystrom says (*ibid.*): "Untruthful advertising is not peculiar to department stores. Specialty stores have sinned in this respect as much as department stores, differing only in the degree to which they have used advertising." And again (p. 249): "Truthfulness of advertising is another important factor in the long run. Readiness of the firm to back up every statement made is the first principle in successful merchandising, not only in the mail order business, but in every other retail business as well. . . . It is probable that any misrepresentations which occur in the advertising matter of most of the large houses, at least, are due to error, rather than policy."

24 It is argued that the retailer's right to reduce prices still remains as to unbranded goods and goods upon which manufacturers do not care to maintain prices. If the effect of legalized price maintenance were to increase greatly the number of advertised brands, the chances are that the price freedom of the retailers would decrease proportionately. And if there is no increase in the number of brands, either because of the controlling position of those already in the field or because of the fact that the majority of manufacturers neither need nor care to use the power given them of fixing resale prices, public interest would be still more opposed to the legalization of price maintenance.

attraction which a store can offer; there are people who prefer to trade where the policy of the establishment is low prices, even if the service rendered is inferior in amount to that offered elsewhere where prices are also higher. Excessive cuts in prices are rare, and the cutter, unless he cuts prices maliciously, may be hurting himself more than any one else.[25]

Fixed resale prices are open to the fundamental objection that they do not take into account the unquestionable variations in the costs of distribution as between different middlemen in the same localities or as between middlemen in different localities.[26] That such differences exist there can be no doubt. The resale price selected by the manufacturer, if selected with reference to those who have high costs of production, will be unduly large for those who are more efficient; while if a lower level be selected, the margin will be unsatisfactory to many retailers whose goodwill the manufacturer is anxious to retain. The retailer under ordinary conditions has the choice of two policies to secure public approval; either of rendering service to the consumer in delivering a commodity to a consumer at a higher price, or of giving the customer less service and charging a lower price, *i.e.*, high price plus much service versus low price plus less service. The common chain store policy of no credit extensions and restricted or no delivery would be impossible under a system of fixed prices, because of the lack of the counter attraction of lower prices as an inducement to consumers to do without the service.

Further, price maintenance does not recognize the essential character of the work of the middleman.[27] Much peculiar economic reasoning is aired in the discussions, to the effect that the dealer is not the principal, but the agent of the manufacturer.[28]

25 Upon this point see testimony of Mr. Ames, before the Federal Trade Commission, reported in *Women's Wear,* Nov. 17, 1917.

26 *Cf.* testimony of J. M. Barnes of Marshall Field & Company, Report II, pp. 79 *et seq.;* E. A. Filene, *ibid.,* pp. 209 *et seq.*

27 L. H. Haney, American Economic Review, vol. VI, no. 1, Supplement, p. 185; W. F. Gephart, *Some Aspects,* etc., p. 169. Testifying before the Federal Trade Commission, Mr. Colgate is reported to have declared that the retailer's goodwill is of no value to branded goods. (*Women's Wear,* Nov. 3, 1917.)

28 A statement of this idea is to be found in the record of the recent hearings before the Federal Trade Commission in the testimony of W. H. Ingersoll. Reported in *Women's Wear,* Oct. 6, 1917, pp. 17-18. Mr. T. T. Ausberry in a brief reprinted in Report II, pp. 326 *et seq.,* says that under price maintenance the retailer is made the agent of the manufacturer without the benefits of agency.

Price maintenance is essentially a proposition to allow manufacturers to fix the margin to be granted to retailers. It does not seem reasonable to suppose, however, that manufacturers are in a better position to select correct prices for goods than are retailers in competition with each other. And the selection of prices for the retailer, while it lessens competition in price, also lessens in part the stimulus to change, the incentive to greater efficiency. The dulling influence of price maintenance would in the long run react to the detriment of the retailers themselves as well as to the public at large.[29]

A generalized system of price maintenance would in all probability not have the ultimate result of decreasing the costs of distribution. The amount of economically wasteful advertising, *i.e.*, the advertising not calculated to educate the public or create a new demand but simply to bring about the transfer of business from one advertiser, would be increased. At the same time, the margin allowed for retailers and jobbers in the fixing of the resale price would in the long run be fixed by competitive forces at an amount sufficiently high to secure their goodwill and coöperation.[30] Price maintenance, by increasing the margin of profit to the small dealer, implies the desirability of maintaining in our distributive system by artificial means members who are not able to compete with others in the same work. The ultimate elimination of the inefficient, both among distributors and among manufacturers, is a necessary accompaniment of progress in production as

29 A system of fixed prices would not make the retailer any more efficient or more able to analyze his costs. *Cf.* W. F. Gephart, American Economic Review, vol. VI, no. 1, Supplement, p. 191; testimony of Professor Samuel McCune Lindsay before the Federal Trade Commission, reported in *Women's Wear,* Oct. 4, 1917, p. 17.

30 The argument that a lower margin on advertised goods is as profitable to retailers, because of ease of increasing volume, as a higher profit on unbranded, unadvertised goods assumes that retailers are able to secure the greater volume. It is evident that in the absence of increase of total expenditures by the public, increase in the volume of sales by a retailer of a certain advertised article can take place only by shifting of demand from other advertised brands, from other articles or from other stores to the particular article at the particular store. Such shifting would bring no net gain to retailers as a whole, and might involve loss. The assumption of comparative stability in total expenditure for different classes of articles by consumers is more reasonable in view of the slowness with which real incomes rise than the statement that retailers generally could benefit by increased volume of sales.

well as in distribution. If price maintenance aims to maintain the present marketing system,[31] it must provide for at least the customary rate of profit now received by distributors; otherwise the goodwill of distributors will not be secured. If price maintenance does not operate to retain it, the argument of price maintenance advocates concerning the beneficial results of the policy to the small independent retailer loses its force.

Price Maintenance and the Consumer

Unless consumers can satisfy their wants on more favorable terms under a legalized system of price maintenance than under the existing state of price freedom, the adoption of the policy is not justified.[32] The consumer is interested in getting the most out of his income; to benefit most he must get as high a quality as possible at as low a price as will afford the necessary encouragement to continued productive effort. Quality cannot be dissociated from price in arguments as to the result of price maintenance or price cutting upon the consumer. It is alleged that price maintenance benefits the consumer because it furnishes him with the opportunity of securing standard brands, or identified articles of fixed quality, which are economical because they save him time, money, and effort, besides furnishing a standard for comparison. Identified goods are therefore declared to be as a class superior to unbranded in quality, and at least as low in price, quality for quality; while price maintenance is held to be necessary in order to assure accessibility to consumers. The last point will be considered immediately.

The argument that as a whole articles of merit will become less accessible under a system of price freedom than under a system of fixed resale prices does not appear to be valid. Price cutting does not ordinarily induce distributors to discontinue handling the articles, unless the goodwill built up by the manufacturer has

31 Professor F. W. Taussig asserts that the influence would be to maintain the *status quo*, AMERICAN ECONOMIC REVIEW, vol. VI, no. 1, Supplement, p. 181; L. H. Haney, *ibid.*, p. 184.

32 Upon the relation of consumers to price maintenance there are numerous references in all the hearings. The controversial literature on the subject contains vigorous assertions, many of which are exaggerated. *Cf.* testimony of Miss Mary Wood (Report III, pp. 283 *et seq.*, later testimony, *Women's Wear*, Nov. 15, 1917); Professor Samuel McCune Lindsay (*Women's Wear*, Oct. 4, 1917); Mr. (now Justice) L. D. Brandeis (Report I, pp. 22, 40); Dr. P. H. Nystrom (Report II, pp. 15, 30).

no substantial basis in the merit of the product;[33] in which case lessened accessibility may not be contrary to public welfare. The saving of time claimed for consumers under fixed resale prices by making it unnecessary to "shop" in order to secure the cut prices is a matter which concerns the consumer's right to dispose of his time as he sees fit.[34] Neither manufacturers nor middlemen are entitled to restrict the right of choice. Further, the statement that identified goods furnish a standard for comparison is an argument for identifying goods, not a reason for price maintenance.[35]

As to quality, it is undoubtedly true that branded goods, identified articles, are often superior. Yet identification is not an infallible guarantee of either good or uniform quality; as Professor Taussig remarks,[36] some identified goods are good, some bad, some indifferent. The attempt is constantly being made to create the impression of superiority in the quality of nationally advertised articles. Even assuming that as a class such articles are superior in quality, it does not follow that price maintenance is necessary to maintain quality. Manufacturers brand goods to secure the goodwill of users; branding should imply the maintenance of quality and the placing of responsibility. Fixed resale prices add nothing to the identification value. If the article is of the sort whose capacity to satisfy wants rests upon its distinction value, it is conceivable that price cutting might so decrease volume of production that costs would increase and likewise the temptation to lower quality; or, in another way, the demand of middlemen for lower prices might have the same effect. But there seem to be few instances in which price cutting has been responsible for serious harm to manufacturers; therefore the inducement to lower quality is not great. Moreover, it is to be assumed that when such identified goods are of superior quality they are sold at a price corresponding; the manufacturer will secure his return in the prices received from jobbers and retailers. Branded goods as one means of standardizing quality are not to be discouraged. The difficulty of determining quality presents a serious problem to the consumer. But modern merchandising

33 *Cf.*, p. 286, above.

34 *Cf.* Statement of Edward A. Filene, published by National Retail Dry Goods Association, p. 4; also Report III, pp. 209 *et seq.*

35 The greater the number of identified goods, the more necessary it would be for the consumer to judge quality as in the case of unidentified goods.

36 American Economic Review, vol. VI, no. 1, Supplement, p. 175.

inclines more and more to the opinion that the public is not as gullible as some discussions of price maintenance seem to imply.[37] Distributors have learned that continued success can be attained only by following the same upright policies which manufacturers declare compel them to give the public a good product at a fair price.[38] Standardization is not a reason why the manufacturer should be empowered by statute to fix resale prices, though in certain cases interference by the state has been found advisable, *e.g.*, in the pure food and drug laws.

Whether prices of identified articles are higher than those of unidentified articles of similar quality and character, is likewise a point upon which no more than a general statement can be made. It seems to be a general opinion that identified articles are higher in price than unidentified, but it is as stoutly maintained by advocates as denied by opponents that the higher price is no more than sufficient to offset the higher quality and greater convenience.[39]

Resale prices of identified articles fixed by the manufacturer are based upon his calculations as to his own best interests. To use the terms popularized by Shaw, he has before him three

37 No valid argument for price maintenance can be based upon the gullibility of the public. If the public is easily deceived, identified goods could be foisted on consumers at high prices; in such a case protection would be needed by the consumer against the manufacturer as well as the retailer. If the public is not gullible, manufacturers may rest assured that if they produce an article of merit, price cutting will not destroy their market; consumers will insist upon securing the article identified by brand.

38 Extracts quoted in Nystrom, p. 204, illustrate this. "Advertisements of bargains are still printed, but the public is almost as impervious to them as the side of a battleship would be to a battery of pea shooters," and the statement of George Hough Perry, former advertising manager of Wanamaker's and Gimbel Brothers, who is reported to have said, "Bargain sales are passing rapidly into the limbo of exploded ideas, that all future tendencies will be toward emphasizing not price, but what can be had for the price."

39 For instance, see statement of Cyrus B. Miller of the Federal Food Board of New York State to the effect that "on the average, advertised packaged goods cost at least 35 per cent more than the same in bulk." New York *Journal of Commerce and Commercial Bulletin,* Jan. 22, 1918. The majority statement in the *Report of the Chamber of Commerce of the United States* contains the assertion (p. 22) that in pushing identified goods upon which prices have been maintained "the consumer is assured a maximum of return for a known outlay." The course of automobile prices furnishes the stock example of the tendency in industries in which prices are maintained; but other factors will readily suggest themselves as accounting more satisfactorily for the lowered prices.

choices—the market price, the market plus, and the market minus.[40] However, in most lines, a price fixed at the outset corresponding to the market price would with the fluctuations in market prices become either market plus or market minus. If a market plus price is selected, either by conscious choice or by the decline of market prices upon similar articles, then it is necessary for the manufacturer in order to maintain or increase the volume of sales to give the impression in some way that for the excess over the market some additional service is rendered; the impression is created by various forms of salesmanship, especially advertising. Since the quality of many goods is indeterminate, not easily judged even by experts, advertising on an extensive scale may enable a concern to continue the market plus price without diminution of volume of sales in competition with other similar goods. If the market minus price is selected, the manufacturer hopes by cutting down his margin and lowering the price to the consumer practically to inhibit competition except on the same plane. The manufacturer in this case rests his claim to patronage upon the fact that he is giving more to the consumer than the market dictates.

Unless the manufacturer is successful in reducing his marketing costs, there is little opportunity for selecting a market minus price. The price selected for sale to consumers must include (a) the manufacturing and marketing outlays of the maker of the identified article, (b) the manufacturer's profit, and (c) the margin for middlemen. Examining these items, it becomes apparent that according to previous reasoning[41] there would probably be little change in the costs of manufacture traceable to fixed prices. Again, it is not reasonable to assume that manufacturers of identified articles are more willing than business men in general to forego profits; in fact, they advocate price maintenance as a means of stabilizing and increasing profits. Further, the margin selected must be sufficiently large to allow for costs of distribution, plus an amount sufficient to secure the goodwill of jobbers and wholesalers.[42] The manufacturer may feel that by

[40] A. W. Shaw, *An Approach to Business Problems*, pp. 234 *et seq.*

[41] See page 288, above.

[42] Mr. F. W. Nash of the General Chemical Company says: "To make the specialty attractive to retailers, it must bear a sufficient profit to make the net margin attractive in comparison with other brands or unbranded goods." *N. Y. Journal of Commerce,* May 8, 1916. *Cf.* also testimony of Mr. William H. Ingersoll before the Federal Trade Commission (reported in *Women's Wear,* Oct. 6, 1917, p. 18).

national advertising he has performed much of the selling function, and therefore the margin to middlemen need not be so great as on ordinary goods; yet under a generalized system of price maintenance a smaller margin will not secure the goodwill of the retailer. Consequently an allowance will be made which will give a satisfactory margin to the majority of middlemen; one perhaps not satisfactory to the least efficient, but one that will represent more than is necessary for the most efficient distributor; in short, at least as large as the margin which would be fixed by competitive prices without maintained prices.

Finally, it does not seem reasonable that under a legalized system of price maintenance the marketing costs of the manufacturer, including advertising costs, would be lowered, so as to make possible lower consumers' prices. The consumer must bear eventually the outlays of the manufacturer for disposing of his product; he must therefore assume the burden of advertising. From the point of view of public interest the problem is as to whether the methods of distribution which would be adopted by manufacturers under a system of maintained prices would result in an increase or decrease in the cost of distribution per unit of product. Many individual instances have been cited in which the unit cost of distribution for a particular concern has been lowered following an extensive advertising campaign.[43] From an economic point of view, however, advertising must be differentiated according to its effects. Some advertising undoubtedly increases total demand; other advertising merely causes existing buyers to transfer their purchases from one concern to another. The former may have some effect upon costs of distribution, lowering them for individual concerns, perhaps for all concerns in that line. The economic value of the latter is doubtful. Though lower costs to certain concerns may ensue, advantage to the public requires that the average costs be lowered and that the public benefit by the lower costs; neither of which is assured by such advertising.

If we assume a great increase in the number of identified and branded articles under a system of maintained prices, the consumers' interest becomes clearer. The purpose of advertising is the creation of goodwill, to establish a preference in the minds of purchasers for a particular article. The goodwill is a differential advantage which one producer possesses over other producers of similar articles. When many producers advertise, advertising

[43] P. T. Cherington, *First Advertising Book,* ch. XIII.

must be continued and increased not only to secure a differential advantage but to prevent being placed at a disadvantage. National advertising by one firm exercises as much pressure upon the manufacturers of similar products to advertise as price cutting does to compel other sellers to cut prices. Competition in the amount of advertising in order to keep a place in the market will involve a great deal of the sort of advertising which has no other effect than to increase the net costs of distribution. The concern whose advertising expenditures were largest would secure the goodwill, other things being equal. And the net result would not be lowered prices to consumers.

Fixed uniform prices deprive the consumer also of a possible share in the benefits of efficiency of certain retailers; neither can the consumer reap any advantage of location.[44] To many persons reduction in price for a given quality is a more desirable benefit of competition than an increase of service; yet under a system of maintained prices, they would be compelled to pay the same price irrespective of their wishes as to the purchase of service. It remains to be demonstrated that nullification of advantages of location is to the best interests of consumers. Whether transportation charges are paid by manufacturer or middlemen, they are ultimately borne by the consumer. If paid by the manufacturer, the fixed retail price will take no account of location; those nearest the source of supply will have to bear as large a proportion of the total costs of transportation as will far distant consumers. If charges are paid by middlemen, their margin must be sufficiently large to afford a satisfactory profit to those far distant.

The effect of monopoly upon public welfare is exerted largely through price control; it may not be illogical therefore to review briefly the various forms of the monopoly argument used with respect to price maintenance and price cutting. The advocates of price maintenance assert that price cutting leads to monopoly of certain types of distributors.[45] They look upon price cutting as a weapon used by the department stores and chain stores as a means of eliminating competition, just as local price cutting was used by the Standard Oil Company. Granting that some price cutting may be unfair and result in the failure of competitors,

44 W. F. Gephart, *Some Aspects*, etc., p. 168; Statement of E. A. Filene, p. 4.

45 For instance, the majority statement of the *Report of the Chamber of Commerce of the United States*, p. 27.

one may assert that the remedy applied in the Standard Oil case, namely the prohibition of the practice which was found to be socially undesirable, is the proper one, not the legalization of resale prices fixed by the manufacturer. But as stated above, evidence available does not indicate that department or chain stores or mail-order houses are securing monopolistic power, or that competition with them has tended to drive out the specialty store.

Price maintenance, on the other hand, is alleged by others to foster monopoly of producers, especially of large advertising manufacturers.[46] If price maintenance secured to advertisers the desired results, namely the protection of differential advantages constituting goodwill, a powerful concern might conceivably entrench itself so firmly that it would possess practical monopoly in that line. It is true that in the case of few articles are substitutes unavailable. Yet those substitutes may not be a practical influence. Nevertheless public opinion has expressed itself in no uncertain terms upon monopoly and unfair competition. Remedies have been provided for abuses, and general prohibitions imposed upon business practices contrary to public policy. These should tend to prevent the abuses of monopoly under a system of legalized price maintenance. They should be equally adequate to correct the price cutting evil if it is proven to lead to monopoly, contrary to public policy.

Conclusion

Under existing competitive conditions it seems that the adoption of a policy of uniform resale prices would not be in the public interest.[47] In the first place, the assurance of uniform and high quality would not be increased by such a system; present methods of identification are sufficient to secure to the manufac-

46 W. F. Gephart, *Some Aspects*, etc., p. 193. Testimony of Dr. Lee Galloway, Report I, p. 73.

47 In a former study, a historical sketch of price maintenance in the book trade, the writer came to no positive conclusions, but the statement was made that price maintenance possessed distinct advantages for all concerned if the price level chosen were the correct one. Subsequent study was approached with some inclination to favor price maintenance. But it appears now that the selection of the correct level is beyond the power of any class, and that an attempt to select it would be highly undesirable. Barring the question of government price fixation, in public service industries or under extraordinary conditions, competitive forces only can be depended upon to bring about the selection of prices in the public interest.

turer the benefit of goodwill honestly built up. There is no indication that manufacturers of advertised goods are any less successful in obtaining substantial rewards for services performed than any other class of business or professional men; consequently no necessity exists for additional inducement to maintain quality. In the second place, there is no assurance that quality for quality, prices will be lowered under a régime of maintained prices; on the contrary, there are reasons for believing that advanced prices will result. Under competitive conditions, fixed resale prices could have little effect in decreasing costs of manufacture or costs of distribution, while the latter would probably be increased by the impetus given to advertising. Since manufacturers and middlemen would not forego profits any more willingly than at present, the retail price could not be lowered. Furthermore, the consumer is deprived of any advantage of location as well as of opportunity to share in the benefits of variations in efficiency of middlemen.

Though it would probably not tend to save the small retailer if less able to render efficient service than retailing establishments of other types, price maintenance would restrict the channels of competition and would dull the incentive to progress both in wholesaling and retailing.

Legalization of the policy of fixed resale prices would undoubtedly accrue to the immediate benefit of the manufacturers who have built up large businesses upon the basis of extensive advertising and to the advertising interests themselves.[48] But it seems that the public has no more interest or plausible reason for guaranteeing stability of sales and profits to a group of manufacturers than to other interests. The goodwill possessed by manufacturers was built up because they considered it good business to make expenditures for that purpose. That there was risk was not overlooked. Reasoned expectations were that the reward would be sufficient to give return upon investment plus compensation for risk incurred. If loss has materialized in certain instances, legislating to guarantee returns to investments made under such conditions suggests the analogy of passing a law to permit insurance companies to refuse to pay losses because profits were decreased by a small amount of incendiarism.

The proposed bill for price maintenance must therefore be con-

[48] Report II, p. 309; also L. H. Haney, American Economic Review, vol. VI, no. 1, Supplement, p. 188,

demned as legalizing a policy which is contrary to the public interest, for the immediate benefit of a few who demand it but who do not need it. The bill gives power to manufacturers which are not accompanied by adequate safeguards for the consumer and middleman. To provide such safeguards would necessitate government supervision or fixation of prices upon manufactured products, involving questions which cannot be discussed here. Further, if passed, uniformity of enforcement of fixed resale prices would require the enactment of state laws to place intrastate commerce under the same restrictions as interstate. Moreover, it is probable that ways would be devised of evading the law, which would make it illusory, unless the government were to adopt means of enforcement as far reaching as are necessary to secure adherence to governmentally fixed prices. Unless the benefit were very clear, the public would not submit to such restriction.

Every observer and student of business affairs has noted with much gratification the rapid rise in standards of business morality. The tendency of the courts to uphold fair trading in every respect has been reënforced by the growing conviction among business men that unfair practices are bad practices, even if regarded solely from a selfish point of view. The common law and statutory prohibitions now in force as to unfair trading will be sufficient, with the aid of the courts, to deal with abuses of price cutting as effectively as public interest demands. The need will grow less as business continues in its progress toward higher ideals of conduct.

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